Environmental, Social & Governance (ESG) Performance & Financial Distress: An Empirical Analysis of Firms in Emerging Markets

SHORT SYNOPSIS

Submitted in partial fulfilment of the requirement of the degree of

DOCTOR OF PHILOSOPHY

By

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It is the work that is expected to be carried out under the supervision of **Prof. (Dr.) Pooja Kapoor**.

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Abstract

The research investigates the influence of Environmental, Social, and Governance (ESG) practices on the financial stability of companies in emerging markets, focusing particularly on India. The contemporary businesses are more mindful about sustainability in the rapidly changing markets. Companies that incorporate ESG practices in their businesses not only aim to improve profitability but also reflects their responsibility & accountability towards the society and environment. However, there are many problems in implementation of ESG practices in India, but once implemented it can significantly help in value generation and develop credibility of firms in emerging markets. Using secondary data from NIFTY 100 companies between 2010 and 2021, the research aims to examine the relationship between Environmental, social and governance factors, financial soundness & distress level of companies. The analysis is done using both descriptive and inferential statistics, including correlation and regression tests. Drawing on Stakeholder Theory and the ESG Fraud Triangle Theory, the study looks at whether responsible ESG practices help companies strengthen transparency, improve governance, and build trust among stakeholders. The findings suggest that strong ESG performance often goes hand in hand with better financial resilience. However, it also appears that some financially stressed firms may exaggerate their ESG activities to maintain their positive public image. Overall, the research highlights dual benefit of role of ESG practices-by acting as an early warning signal and a tool to assess & improve overall financial heal of the companies in emerging markets.

Keywords: ESG, Financial Distress, Emerging Markets, Sustainability Reporting, Stakeholder Theory, India

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1. INTRODUCTION

1.1 Research Background

Environmental, Social, Governance (ESG) is one of the measures that firms and businesses have been undertaking in recent times with the potential trend of increasing demands for sustainability for emerging markets. International goals and adoption of emission reduction and integration of green changes have instigated the importance of consideration of inclusion of ESG scores of companies as much as their financial activities. India, as an example of an emerging market, could be seen as one of the countries that has implemented a compulsory approach to ESG engagement (Arun *et al.* 2022). The financial distress of firms and organisations can cause businesses and firms to face financial problems such as bankruptcy, debts, equity inefficiency and lack of current assets, and could be caused by several reasons including economic distress or performance decline (Younas *et al.* 2021). ESG is focused on reporting the impact of organisations on the goals towards sustainability.

There is also a possibility for corporate social responsibility disclosures that often involve ESG scores and engagements being involved in the development of financial reporting quality of the firm (Arun *et al.* 2022). Hence, trying to realise the relationship between ESG scores and financial distress of a company is identified as an effective form of application that would be beneficial in terms of expanding into the subject of the ESG and financial distress relationship. It is considered that ESG has a predictive capability in terms of correctly identifying financial distress (Citterio and King, 2023). This is likely the case due to the factor of ESG having an impact on the aspect of classification of the distressed and defaulted business opportunities and businesses such as banks as healthy, strongly reducing the likelihood of misclassification.

The debate regarding the level of informativeness of ESG scores as a prerequisite for ascertaining companies and their ESG activities as well as the financial performance of companies. The inclusion of ESG scores as an evaluation measure is subjected to the believed construct of financial performance being reflected under the idea of financial performance having an effective relationship with ESG. Such a construct also subjects the use of ESG ratings and scores as a measure for investment activities regarding long-term and “operational corporate” investment-related decisions (Lohmann *et al.* 2025). However, it was observed that the potential lower likeliness for companies to misclassify poor financial performance with the implementation of ESG is also a considerable aspect. However, it must also be noted that ESG

score management by financially distressed companies could contribute towards the reduction of the validity and credibility of ESG scores as a reliable source.

Increase of demand and focal shifts of the target towards the goal of achieving sustainability is becoming apparent in the case of emerging markets. The recognition of corporate responsibility of catering to the demands of disclosures addressing business practices that are minimal on the social and environmental impacts, and the follow up of disclosure policies addressing the need for change of traditional financial disclosure being changed to meet the requirements of addressing the needs for satisfying the stakeholders, policymakers and investors (Persakis *et al.* 2025). ESG could be considered as one of the measures that are connected with such non-financial disclosures that are identified to have a reach on several categorical reportings that go beyond financial reportings. ESG disclosure is considered as a non-financial disclosure for catering a broad audience of suppliers, customers, investors, and governments among others through the integration of the reporting into a versatile instrument for fulfilling the purpose of the disclosures to provide information on non-financial aspects of financial activities. The study explores the relationship between the ESG and financial disclosure.

Problem Statement

The study considers exploring and evaluating the research problem of ESG and financial distress of businesses in emerging markets of developing countries such as India. The financial performance of industries and companies through several sectors has an impact on the development of the economy. However, the trend of financial disclosure not being entirely enough for instigation of the influence of making investment and engagement decisions from the investors and other respective stakeholders of businesses in an emerging market. India is one of the economies with emerging markets to have made mandatory non-financial disclosure reporting on the sustainability, environmental, social and governance activities and engagements from the side of the companies. It is noted that financially distressed companies tend to present higher ESG scores, with financially unrestrained companies being more prone to have better opportunities to practise ESG objectives (Lohmann *et al.* 2025). The integrations for non-financial disclosure require reporting on the non-financial engagements as an addition to the traditional financial reporting of the conditions of companies that enable them to take part in sustainability and ESG-related activities.

Figure 1: Trends of GDP drop in India

(Source: Buchholz, 2021)

The financial performance and distress of an emerging market could be seen through the aspect of the financial condition of the economy of the said emerging market. For instance, in the case of India as an emerging market, it could be seen to have a difficult condition in terms of economic developments. As of the financial year of 2020/21 to 2021/22, India had developed the trend of around 20.1% GDP growth since the first GDP dip in the financial year 2020/21, however, only accounting for another GDP dip with GDP at around 443.8 billion USD, a mild improvement of 369.4 billion USD from the earlier dip (Buchholz, 2021). The above could imply the struggling condition of the financial distress of the market and industries in the Indian economy.

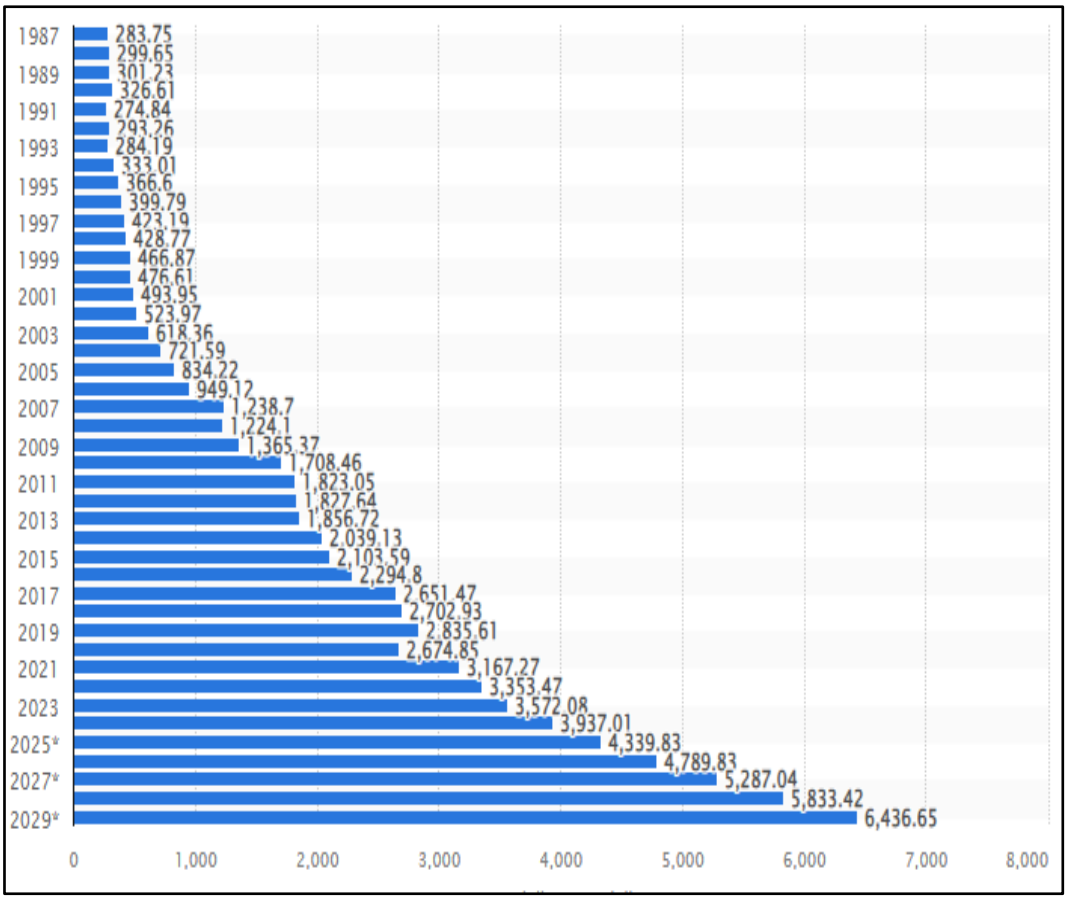

Figure 2: Record of GDP in current prices (in billion USD)

(Source: O'Niell, 2025)

The GDP, as a traditional indicator for financial economic growth for an emerging market such as India could present trends for potential financial development or declines. As such, in comparison, it can be observed that the financial development for the emerging market is dependent on the operating businesses on the financial contribution of growth through different years of development with potential predictions of economic developments. As per the above graphical presentation, the GDP had shifted from 2,674.85 billion USD in 2020 to 3,572.08 billion USD in 2023 and is predicted to amount to 4,339.83 billion USD by 2025 (O'Niell, 2025). Such financial developments indicate the potential for businesses to expand within recent years with the possibility of increasing financial growth of the Indian economy.

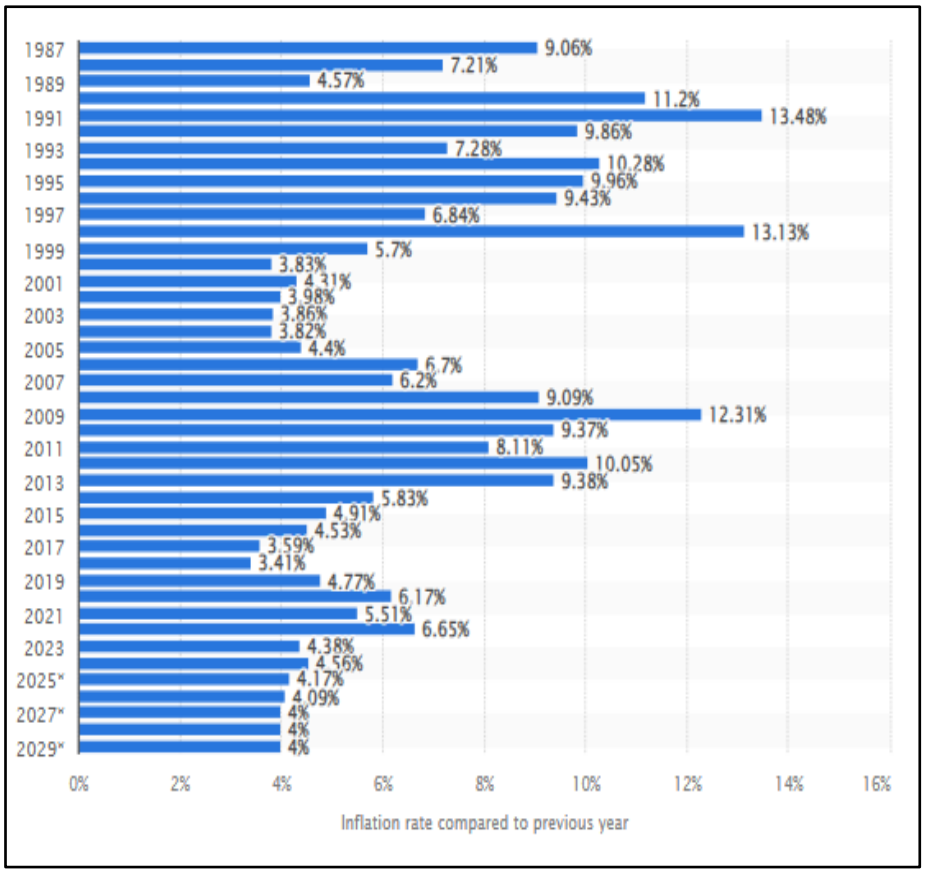

Figure 3: Inflation Rates in India

(Source: O'Niell, 2024)

Though there are indications that there is a possibility for financial growth, other economic indicators such as inflation is identified as an aspect for understanding the potential of existing financial problems that different industries might face. As in the year 2020, the inflation rates had been 6.17%, which shifted to 5.51% in 2021, and 4.38% in the year 2023, with the forecasts of declining inflation rates by 2025 to around 4.17% (O'Niell, 2024). Changes in inflation could impact the drive for sustainability, as it has been observed that there is the instance of increasing inflation and interest rates having an impact on sustainable funds and the approach of greenwashing claims affecting the success of sustainable funds (Ross, 2023). Such instances are more probable to occur due to the volatility and uncertainty of the market as an aspect contributing to the development of the environmental, social and governance related investments and financially signifying progress. The shifting tendency for the investors and stakeholders examining non-financial aspects due to market uncertainty also makes ESG scores and non-financial disclosure reporting essentially connected.

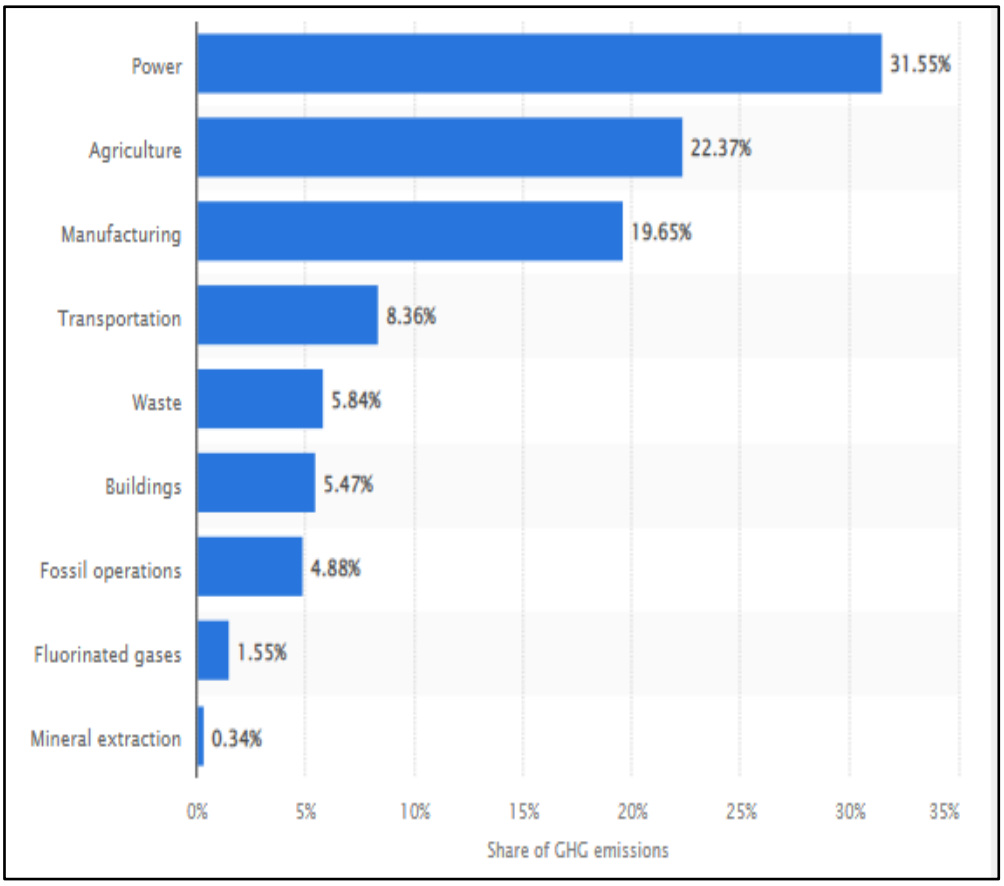

Figure 4: GHG emissions in India in 2022, sector-wise distribution

(Source: Tiseo, 2024)

As ESG scores and reporting gio beyond the development of the evaluation and reporting for financial elements of disclosure, it allows the investors to examine and make investment decisions into companies that contribute towards more sustainable businesses and companies. As of 2022, the power industry has been contributing the most to the greenhouse emissions in India with around 31.55% of GHG emissions, while agriculture industry has contributed around 22.37% of the total GHG emissions in India (Tiseo, 2024). Non-financial and sustainability components such as greenhouse gases emissions are among some of the non-financial aspects covered under the sustainability driven disclosure.

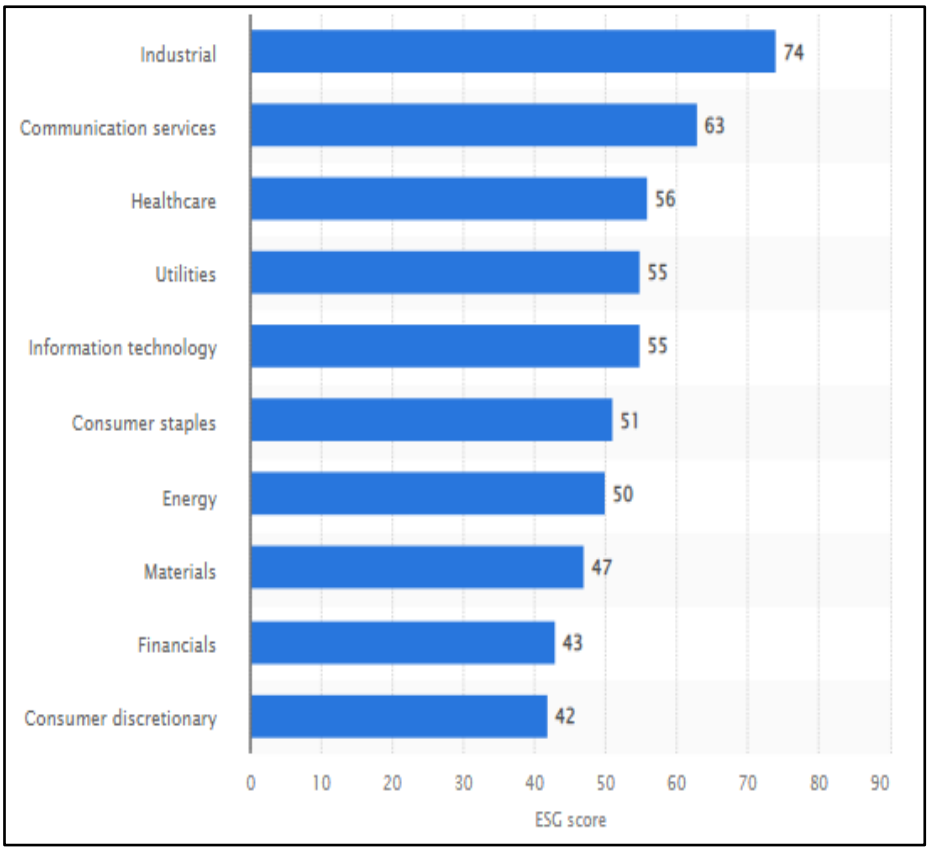

Figure 5: ESG composite score of NIFTY 50 in India by sector, 2021

(Source: Keelery, 2024)

The financial and non-financial aspects required for reporting could contribute to the observation of the influences that these have on the investors in making investment decisions, as well as influencing the stakeholders. As of 2021, several industries have been observing an increasing growth on ESG composite scores. In 2021, it was seen that industrial companies had the highest ESG composite scores, coming at 74, while communication services and healthcare came second and third, with ESG composite scores of 63 and 56 respectively (Keelery, 2024). Financial distress and performance are closely involved with the aspect of ESG as the capacity for financially supporting the development of ESG activities in companies. Exploration of the relationship within ESG and financial distress in context to emerging markets are considered

2. LITERATURE REVIEW

The impact of ESG on financial distress in emerging markets has several implications, with most commonly perceived of them being the impact that ESG has on the reporting of financial performance of companies as well as addressing non-financial components. As per the study by Badrudin *et al.* (2025), financial distress is a critical challenge that is often considered through the aspect of inadequacy of the firm's financial distress. However, there is also the consideration of the fact that non-accounting aspects such as poor management and context to managerial responsibility such as ESG and corporate social responsibility reportings are also considered as insightful elements towards evaluation of financial stability and financial distress for businesses.

Prediction of risk of financial distress in companies is regarded as a central theory of finance and industries given companies are capable of facing challenges then credit defaults day restructuring or bankruptcy due to financial circumstances. In the study by Song *et al.* (2024), sector companies such as energy companies are increasing pressure to work on compliance with policy and sustainability goals of reducing global carbon emissions contributions. ESG performance reporting is regarded to have an impact on corporate financial distress risk in the energy sector. Further ESG rating is capable of illustrating potential companies falling into financial distress.

As of recently financial scandals and difficulties have caused stakeholders and investors to lose trust and confidence in companies that have post-organisations to integrate socially responsible corporate conduct Strategies and patterns. According to the study by Almubarak *et al.* (2023), the reasoning behind socially responsible corporate conduct being adopted as disciplinary actions protection for reputation and status security is considered one of the major reasons associated with ESG sustainability awareness promotion adoption and reporting. Studies have suggested that the United Nations recommend that all companies to adopt ESG practices by the year 2030. Some of the major motivations that work behind ASG reporting of companies include investment performance, product strategy, ethical considerations and demand from clients.

Corporate fraud is becoming increasingly concerning for several involved actors such as investors and regulators. In the research by Harjoto *et al.* (2025), the outbreak of corporate scandals and financial crises implies the inclusion of regulation as a way to reduce opportunity

and incentive for committing corporate fraud. Studies suggest that the corporate ethical culture is impactful in terms of determining the security of corporate fraud as a predictable inclusion. However, it must also be noted that regulatory restrictions have not been as efficient in terms of the prevention of corporate fraud. Organisational cultures are capable of influencing ethical analytical behaviour that might also influence the instigation of committing corporate fraud.

ESG criteria are identified as a standard metric for companies and investors to consider in terms of operation and investment-associated risk impacts and opportunities related to decision-making. In the opinion of Mukhtar *et al.* (2025), ESG is gaining significant attention and a global level and it is used as a matrix for the evaluation of company performance and investors and other stakeholders utilising ESG-based information to recognise the companies' environmental and social practices advocacy into their decision making. ESG is considered an industry standard for application by government financial firms and variations that demonstrate a constant contribution to responsible investment channels. The trend of trying to adopt technological advancements and other forms of advancements also furthers on inclusion of government finance forms and corporations regarding responsible investment-related contributions.

Environmental social and governance-oriented investments have been gaining in demand in recent years. As per the study by Sun *et al.* (2024), it is mostly believed that human goodwill and the perception of socially responsible firms are capable of being rewarded in the capital market. Investors predict high sustainability firms have a better future performance tendency. Highly toxic emission-producing companies tend to generate higher stock returns than other counterparts thereby attributing towards the risk premium that is related to the environmental policy risk that such companies are facing.

For a number of years, there has been a visible increase in the frequency and probability of corporate fraud. Harjoto (2025) mentions that the implementation of corporate social responsibility (CSR) can be a major factor in lowering the occurrences of such fraudulent acts. The reason behind this is to a great extent the fact that CSR systems derive from ethical principles, social responsibility, and maintain good relationships with stakeholders, all of which encourage honesty in organizations.

One of the ways to reverse corporate fraud is to concentrate on the improvement of ethics among the corporate leaders, mainly managers, and to implant ethical norms in the strategic decision-making process. Managers are now more and more influenced by ESG (Environmental, Social, and Governance) factors in their overall business strategy and firm performance. The use of ESG elements in the business world has led to the major changes in transparency, corporate reporting, and accountability. As per Arvidsson and Dumay (2022), the adoption of sustainability accounting and disclosure practices is a way to connect the gap between scholarly research and business practice, thus, creating real value for corporate sustainability. The critical role of corporate ESG information plays an important role in Assassin the company's long-term performance and companies are required to assure providing more information with relevance.

Reporting quality has an important aspect in terms of building an influential foundation of communication and trust among stakeholders and companies. The study by Merter and Özer, (2024) noted that investors are more prone towards effectively analysing the financial health and return of a firm through accurate, reliable and transparent financial information. There is also the possibility of misleading positive images in financial information by several firms. Such trends for financial reporting quality make it more significant for ESG activities to become essential for the current business environment and global economy.

Corporate failure prediction is recognised as a major issue in terms of managerial decision-making for both financial as well as non-financial companies. As observed in the study by Citterio *et al.* (2024), business failure and financial distress are mostly regarded by several wording sciences for multiple intensities. ESG variables are often considered to be capable of predicting financial distress. Studies imply that non-financial performance has been gaining a progressive increase in terms of significance among companies and their holders as well as regulators. Credibility loss during the financial crisis has caused banks to integrate social responsibility actions and improve transparency and compliance with sustainability standards.

3. DESCRIPTION OF BROAD AREA

Stakeholder Theory

Stakeholder theory is considered to be a theoretical framework that is associated with the application of ESG reporting. This theory implies the idea that a successful company is capable of aligning the interests of all stakeholders and being more sustainable (López-Cabarcos *et al.* 2025). This theory implies that companies do not focus on Profit maximisation as a sole interest but also work on the interest of other stakeholders except shareholders as well. This is mostly applicable to ESG disclosures given that the popularity of ESG disclosures also contributes towards the inclusion of stakeholders and investor demand responses as well as the practice of establishing credibility and reacting to competition and crisis.

ESG Fraud Triangle Theory

ESG fraud triangle theory implies the inclusion of three factors acting as enabling forces for fraud commitment. The driving factors behind fraud commitment include pressure, opportunity, and rationalisation and this theory's application implies that ESG fraud is capable of occurring due to pressure, opportunity, and rationalisation (Tarjo *et al.* 2024). This application implies that stress due to internal and external pressure as well As pressure from stakeholders and corporate groups are capable of causing ESG fraud. Opportunity governance problems provide options for ESG fraud to be conducted. In terms of the rationalisation factor, the aspect of someone committing fraud is regarded as one of the causes with organisational culture being one of the major causes in respect to this. Hen fraudulent ed reporting and quality can also be hampering the predictive power of ESG activities and reporting on the financial distress of companies.

4. OBJECTIVE AND HYPOTHESIS OF RESEARCH

The research study has the following objectives and questions intended for exploration:

Research Objectives

RO1: To explore the influence of ESG on financial distress in an emerging market

RO2: To identify the different components involved with ESG's impact on financial distress observations

RO3: To explore NSE 100 companies' financial distress in relation to ESG scores

Research Questions

RQ1: What is the influence of ESG on financial distress in an emerging market?

RQ2: What are the different components involved with ESG's impact on financial distress observations?

RQ3: What is the condition of NSE 100 companies' financial distress concerning ESG scores?

Research Hypothesis

H0: ESG does not have an impactful role in ascertaining the financial distress among companies in an emerging market

H1: ESG has an influential role in determining financial distress among companies in an emerging market

5. RESEARCH METHODOLOGY

Research Strategy

The research strategy includes the selection of secondary quantitative data collection and research. The strategic application also includes data being collected from secondary sources they were making this app a quantitative study.

Research Instruments

The study would mostly be collecting information from published sources such as websites, reports, articles and documents. This includes data collection from financial information indexes on ESG score indexes. The research instruments involve secondary quantitative data that exist in their studies. This would also imply the application of Data Collection methods involving

Sample of Study

The sample population of the study includes implementing purposeful sampling as a strategy for selecting an appropriate target audience to collect data from. The sample population would be India as the emergent market and Nifty 100 ranking companies as the prospective studies of the study.

Data Collection Method

The data collection process includes a collection of secondary quantitative data with quantitative information being collected from secondary data sources surface published articles, websites and document reports. The data collection procedure would involve gathering of relevant information within the time frame of 2010/11 and 2020/21 as the tentative time frame for data collection

Data Analysis Method

The data analysis procedure would involve descriptive analysis and inferential statistical analysis of the quantitative values that would be gathered from the selected data sources for the statistical data evolution. The data analysis procedure would involve the evaluation of the information using several forms of statistical data analysis methods that include descriptive statistics, correlation and regression.

Research Design

Selected Research Design

The study will be following Exploratory Research Design as the designated research design for the study.

Conceptual Framework

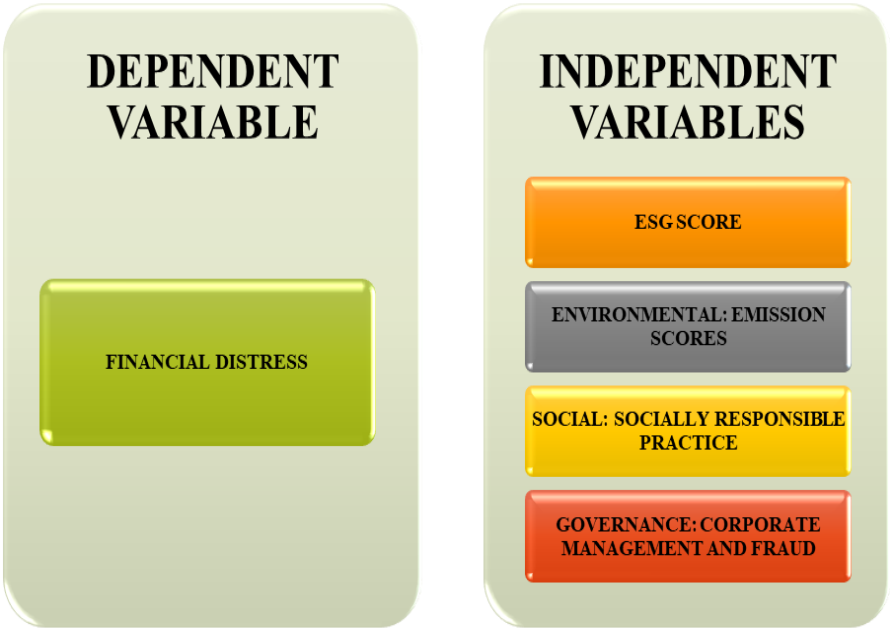

Figure 6: Conceptual Framework

(Source: Self-developed)

The above image illustrates the dependent and independent variables of the study. The dependent variable includes financial distress that could be evaluated through several components including financial performance. In the case of independent variables, it includes ESG score environmental factors as emissions cause among others social factors including socialist practice and governance factors including corporate management and fraud issues.

6. EXPECTED OUTCOME OF THE RESEARCH

Research Gap

The study has focused on conducting a well-organised secondary data collection through the gathering of secondary quantitative data and their analysis using different methods. This process includes proper development of theoretical implications upon the study areas of ESG goals and their implications upon financial soundness of different companies assigned under NIFTY 100 index in Indian Stock Exchange. However, the researcher has remained unable to conduct a typical analysis of the primary quantitative study that could provide the researcher with an idea about the present implications of the ESG goals in the NIFTY 100 indices market, and the stock market stakeholders that have significant implications in their professional lives due to the market variations occurring each day.

Possible Outcome of Research

The study would be a contributing literature into the research subject of ESG scores and activities impacting financial distress of companies in an emergent market. India is one of the emerging markets as of recently and the potential outcome that research night contributes towards is the option of expanding on the research subject of identifying the potential impact that ESG has on financial performance reporting. This makes the study to be opportunistic for future purposes on research regarding ESG factors impacting financial development.

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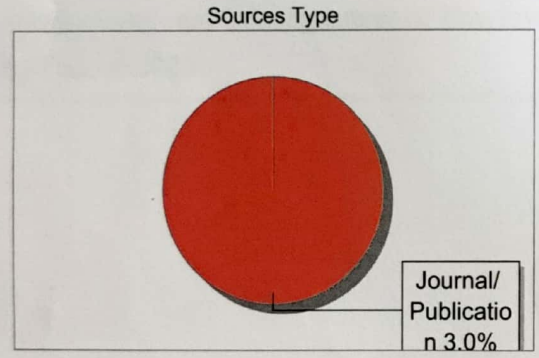

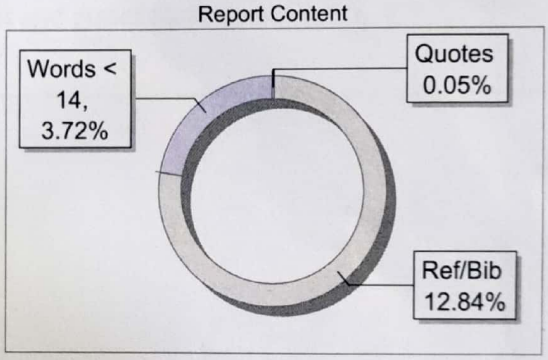

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Environmental, Social & Governance (ESG) Performance & Financial Distress: An Empirical Analysis of Firms in Emerging Markets

SHORT SYNOPSIS

By

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Declared as State Private University vide Haryana Act 26 of 2014

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Abstract

The research investigates the influence of Environmental, Social, and Governance (ESG) practices on the financial stability of companies in emerging markets, focusing particularly on India. The contemporary businesses are more mindful about sustainability in the rapidly

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changing markets. Companies that incorporate ESG practices in their businesses not only aim to improve profitability but also reflects their responsibility & accountability towards the society and environment. However, there are many problems in implementation of ESG practices in India, but once implemented it can significantly help in value generation and develop credibility of firms in emerging markets. Using secondary data from NIFTY 100 companies between 2010 and 2021, the research aims to examine the relationship between Environmental, social and governance factors, financial soundness & distress level of companies. The analysis is done using both descriptive and inferential statistics, including correlation and regression tests. Drawing on Stakeholder Theory and the ESG Fraud Triangle Theory, the study looks at whether responsible ESG practices help companies strengthen transparency, improve governance, and build trust among stakeholders. The findings suggest that strong ESG performance often goes hand in hand with better financial resilience. However, it also appears that some financially stressed firms may exaggerate their ESG activities to maintain their positive public image. Overall, the research highlights dual benefit of role of ESG practices-by acting as an early warning signal and a tool to assess & improve overall financial heal of the companies in emerging markets.

Keywords: ESG, Financial Distress, Emerging Markets, Sustainability Reporting, Stakeholder Theory, India

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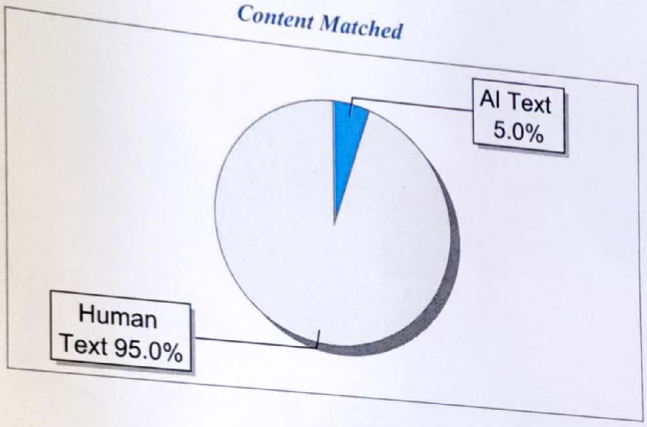

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